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STATE FOR EB/IFD/OMA
TREASURY FOR DO/IDD AND OUSED/IMF
SECDEF FOR USDP/DSAA
PASS EXIM FOR CLAIMS -- EDELARIVA
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SUBJECT: PARIS CLUB - SEPTEMBER 2005 TOUR D'HORIZON

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SUMMARY

¶1. (SBU) At the September 2005 Paris Club meeting, creditors agreed that Iraq's recently announced debt restructuring offer to its private creditors was broadly comparable to the deal it received in the Paris Club last year. Some creditors (Italy, Japan, Italy) suggested that Iraq may not be negotiating in good faith with its private creditors, but the IMF said it was premature to judge whether the Fund's lending-into-arrears policy had been violated, and the Paris Club Secretariat reminded creditors that the issue is not for the Paris Club to decide. The IMF gave a cautious assessment of Iraq's prospects for signing a Stand-By Arrangement by the end of the year, stating that it hoped to commence negotiations in the fourth quarter. Negotiations with Nigeria on a final settlement with the Paris Club are expected to take place in October, if a Policy Support Instrument for Nigeria is approved by that time. Creditors agreed to "freeze the flows" as of September 15, so that any missed payments falling due at the end of the month do not add to arrears. In addition, the Secretariat confirmed that Nigeria is prepared make an additional cash payment toward its 2005 debt service. Other countries on the agenda included Angola, Argentina, Burundi, the Dominican Republic, the Democratic Republic of the Congo, Gambia, Indonesia, Malawi, Peru, Russia, Sao Tome and Principe, Serbia and Montenegro, Sierra Leone, and Sri Lanka. END SUMMARY.

ANGOLA

¶2. (SBU) The IMF reported that the authorities were no longer interested an SMP, but were now eyeing a PSI as a means to a Paris Club treatment. The Secretariat took stock of whether any creditors had cut bilateral deals with Angola to recover some of their claims, and whether any creditors were contemplating new financing. Although no creditor reported cutting a bilateral deal (not counting Germany in 2003 and Russia in 1996), Sweden acknowledged that it recently extended USD 17.5 million in short-term financing, and Italy said it was under tremendous pressure from its export credit agency to resume lending. Creditors agreed that, for the time being, they should refrain from cutting any deals in order to maximize pressure on Angola to reengage with IMF - even though this strategy has been unsuccessful to date. The UK was the most vocal in questioning the wisdom of lending to a country in debt distress.

ARGENTINA

¶3. (SBU) Italy once again was the sole creditor to block a proposal by the Secretariat to send a letter to Finance Minister Lavagna urging Argentina to clear its arrears with the Paris Club. Italy reiterated its argument that a letter to the authorities would signal that there is no hope for repairing relations with the IMF, and that the Club accepts the results of the bond exchange. In response, the Secretariat circulated a revised letter urging Argentina to clear arrears and conclude a program with the Fund. Italy has yet to comment.

BURUNDI

¶4. (SBU) Creditors agreed to provide Burundi a debt treatment on Cologne terms following decision point in July. The agreement will be finalized by mail. (The US is not a creditor.)

Dominican Republic

¶5. (SBU) Creditors agreed that the DR had satisfied the comparability of treatment requirement, clearing the way for

negotiations with the Paris Club next month on a 2005 rescheduling. The IMF reported that the authorities completed a restructuring of commercial bank loans in July and are working to restructure debt to private suppliers. Canada reported USD 1.5 million in post-cut-off-date arrears resulting from a missed payment in August.

DEMOCRATIC REPUBLIC OF THE CONGO

16. (SBU) Creditors agreed to extend the consolidation period of the current Paris Club arrangement through March 2006, in line with the extension of the DRC's Poverty Reduction Growth Facility (PRGF). The current arrangement provides for interim debt relief on Cologne terms. The US announced that we are now in a position to provide interim relief, and that we will continue to seek budget authority to join the consensus on an eventual HIPC completion point treatment. The Secretariat noted that, under the current Paris Club arrangement, some moratorium interest payments are scheduled to fall due in March 2006. Creditors will decide how to deal with these payments as the date approaches, based on the DRC's capacity to pay.

GAMBIA

17. (SBU) The Secretariat will inform the Gambian authorities that the second and third phases of the 2003 Paris Club agreement granting interim debt relief on Cologne terms will not enter into force because the country's PRGF is off track. (The US is not a creditor.)

INDONESIA

18. (SBU) Creditors reported on the status of their bilateral agreements implementing the tsunami debt deferral. The US, Australia, France, and Norway have concluded their bilateral agreements. Several other agreements are nearing completion. Some creditors (Austria, Canada, France, Italy, Korea, Norway, Switzerland) reported that they are charging no or low interest on deferred amounts.

IRAQ

19. (SBU) The IMF gave a cautiously worded assessment of Iraq's prospects for signing an SBA, stating that staff hope to commence negotiations on an SBA in the fourth quarter. When asked pointedly by Sweden whether Iraq was currently off track, the IMF responded that the Executive Board did not declare the EPCA to be off track, but did identify a number of issues that need to be resolved before SBA negotiations can commence.

10. (SBU) Some creditors (Italy, Japan, France) suggested that Iraq may not be negotiating in good faith with its private creditors. The IMF said it had encouraged the Iraqi authorities to negotiate in good faith, as required under the Fund's lending-into-arrears, but that it was premature to pass judgment, since negotiations on an SBA had yet to begin. The Secretariat conveyed concerns raised by some private creditors about the negotiating process, but pointed out that lending into arrears was not an issue for the Paris Club to decide. The US emphasized that Iraq and its advisors had held numerous meetings with many creditors, and that the vast majority of claimants appeared to be satisfied.

11. (SBU) Creditors agreed to extend the deadline for concluding Paris Club bilateral agreements to the end of the year. (To date, only the US and Canada have concluded their bilateral agreements.) On the issue of comparability of treatment, creditors agreed with the Secretariat's preliminary assessment that Iraq's offer to its private creditors was comparable to the treatment it received in the Paris Club.

MALAWI

112. (SBU) Creditors agreed to extend the consolidation period of the current Paris Club arrangement from December 2004 to September 1, 2006, following approval of Malawi's new PRGF last month. The current arrangement provides for interim debt relief on Cologne terms. Malawi is projected to reach completion point in mid-2006 at the earliest. (The US is not a creditor.)

NIGERIA

113. Paris Club negotiations are tentatively scheduled for the week of October 17, assuming a PSI is in place by that time. The Secretariat urged creditors to complete their data reconciliation

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process with Nigeria as soon as possible so that the Secretariat can calculate precisely how much Nigeria owes each creditor once the deal is struck. (The implication that the aggregate figures

could shift pending further data reconciliation is somewhat worrisome.) Encouragingly, creditors did not object to the Secretariat's proposal to freeze the flows as of September 15, so

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that any missed payments at the end of the month do not add to arrears. The Secretariat confirmed that Nigeria is prepared to honor, on a pro-rated basis, its commitment to pay USD 1 billion in debt service in 2005 (above and beyond the USD 12.4 billion cash outlay envisioned under the upcoming deal). If creditors agree to freeze the flows as of September 15, Nigeria would owe creditors an additional USD 450 million in debt service on top of the USD 300 million paid earlier this year. In other matters, creditors agreed with the Secretariat's assessment that Nigeria has already satisfied the comparability of treatment requirement through previous restructurings of its private debt. On the issue of how to score the proposed debt treatment in terms of ODA assistance delivered, the Secretariat informed creditors that the Development Assistance Committee viewed the buyback portion of the deal as a commercial operation, meaning the discount involved should not count as ODA.

PERU

¶14. (SBU) The Secretariat summarized the results of Peru's recently concluded prepayment operation. Peru prepaid a total of USD 1.6 billion to 12 Paris Club creditors, reducing non-ODA principal maturities falling due in 2006-2009 from USD 1.77 billion to USD 197 million. The US and Belgium were the only two Paris Club creditors with exposure to Peru not to have participated in the prepayment operation. (The US welcomed Peru's prepayment offer but did not sign the Agreed Minute for legal and budgetary reasons.)

RUSSIA

¶15. (SBU) The Secretariat summarized the results of Russia's recently concluded prepayment operation. Russia prepaid a total of USD 15 billion to 16 Paris Club creditors (including the United States), reducing its overall Paris Club debt from USD 37.2 billion to USD 22.2 billion. Creditors agreed that Russia had respected the terms of the agreement, thus triggering the agreement's non-securitization provision, which prohibits creditors from securitizing their remaining Russian claims until at least December 31, 2006. Russia said that it had yet to make a decision about any future prepayment operations, but indicated that it has sufficient resources to prepay the balance of its Paris Club debt.

SAO TOME AND PRINCIPE

¶16. (SBU) Following approval of STP's new PRGF last month, creditors agreed to provide STP with a retroactive Cologne treatment, effective from May 2001 to December 2007. The agreement will be finalized by mail. In return, STP will be responsible for making an upfront payment of about USD 1.5 million covering interest arrears and late interest. (The US is not a creditor.)

SERBIA AND MONTENEGRO

¶17. (SBU) The USDEL announced that it had obtained domestic legal authority to support the Paris Club's decision in June to extend S&M's current arrangement (which provides for the capitalization of 60% of interest payments) until the end of the year. The Secretariat will send a letter to the S&M authorities notifying them of the extension and urging them to implement reforms necessary to complete the final review under the country's IMF program.

SIERRA LEONE

¶18. (SBU) Sierra Leone reached decision point in March 2002 and received interim debt relief from the Paris Club on Cologne terms. Interim relief expired in June 2005, when Sierra Leone completed the sixth and final review of its PRGF. Although the authorities hope to have a new PRGF in place next January, the Paris Club cannot formally extend the consolidation period of the current arrangement in the absence of an IMF program. Nevertheless, creditors agreed to bill Sierra Leone as if Cologne terms still applied. (In the case of the US, we will no longer be able to go beyond Cologne terms and forgive 100% of pre-Cologne Summit flows falling due after decision point.)

SRI LANKA

¶19. (SBU) Creditors reported on the status of their bilateral agreements implementing the tsunami debt deferral. Norway and France have concluded their bilateral agreements. A few other creditors have made good progress. (The US expects to finalize

its bilateral later this month.) Norway, Canada, France, and Korea reported that they are charging no or low interest on deferred amounts. In response to Sri Lanka's request for a two-year extension of the debt deferral, creditors agreed that any extension could only take place within the normal Paris Club framework, meaning Sri Lanka would first have to have an IMF program in place.

METHODOLOGICAL DISCUSSION: DE VENECIA SWAP INITIATIVE

120. (SBU) Creditors dismissed Philippine Congressman de Venecia's proposal calling on the Paris Club to conduct debt-for-equity swaps with middle-income countries to help them achieve the Millennium Development Goals. Several creditors characterized the proposal as a "non starter" and stressed that the Club - through the Evian approach - already had the tools to deal with middle-income countries in debt distress. In a related issue, a few creditors (led by Norway, and supported by the UK, Italy, and Russia) thought the Club should consider removing the ceiling on non-ODA debt-for-development swaps. Other creditors (Sweden, Netherlands, Australia) disagreed, arguing that the club was not a development institution. The Secretariat agreed to produce a working paper on the subject.

METHODOLOGICAL DISCUSSION: BREAKAGE COSTS

121. (SBU) Although most creditors agreed with the Secretariat's recommendation that debtor countries should not be forced to pay so-called "breakage costs" in future prepayment operations, and that creditors and debtors should not negotiate bilateral settlements, two creditors (Netherlands, Australia) requested more time to study the matter. The Secretariat agreed to revisit this issue in the future.

METHODOLOGICAL DISCUSSION: EXTENSION OF HIPC

122. The Secretariat encouraged the IMF to work closely with Paris Club creditors to ensure that the data it was using to evaluate potential new HIPC countries was accurate. Japan suggested that the IMF and World Bank may not be taking into account the full extent of Japan's debt cancellation for certain low-income countries.

Methodological Discussion: IDA-administered Loans

123. (SBU) EU creditors agreed that they will not require any payments after November 1 on EU loans administered by IDA and extended to HIPC countries having reached completion point. These loans were previously thought to be multilateral loans but were recently reclassified as bilateral loans subject to Paris Club treatments.

MINIMIZE CONSIDERED.
STAPLETON#